2018 ANNUAL CONSUMER PRODUCTS SPOTLIGHT
M&A trends and private equity deal activity
“Buyers are coming to the table with a lot more information today than they were just five years ago.”

Kunal Bhatt, Director, Transaction Advisory Services
Participants in RSM’s US Middle Market Business Index indicate that, over the past year, they have started the process of passing price increases downstream to customers. However, modeling out how to shift the costs of a tight labor market and increased tariff rates onto the consumer remains a concern even as companies in the consumer products (CP) space become increasingly aware of how trade policies can impact their operations. In this environment, middle market companies that achieve strong branding through social media, and that leverage efficiencies in their supply chains and production cycles through technology to support the digital experience, can position themselves for higher valuations from prospective private equity (PE) buyers. Meanwhile, far more rigorous levels of due diligence have become the norm across the industry over the past five years. This increase in actionable information on acquisition targets is resulting in fewer broken deals despite today’s historically high multiples.
The tightest labor market in a generation has increased pressure on restaurants along with companies in food & beverage, fashion, and retail to improve controls around labor costs. For restaurant operators, RSM predicts that the tight labor market will result in wage growth across the space of 4 percent by year-end. In the food & beverage space, where wages and tariffs are already hitting margins, record-low unemployment has already started to increase transportation costs as the number of truck drivers dwindles, compounding existing distribution challenges. Maintaining a strong floor staff has become a bigger challenge in this labor environment as well. Middle market retailers must continue to manage labor costs by striking the right balance in digital strategy to keep their tech-savvy consumers satisfied.
The preeminent theme among investors entering the new year is the further risk that US trade policy could pose for price inputs. However, middle market CP companies that make good on pledges to implement digital investment strategies will continue to justify their elevated valuations over the near term. Technology investments among middle market companies, buoyed by the Tax Cuts and Jobs Act of 2017 that provided additional bonus depreciation to support increased levels of capital expenditures, include areas such as robotics, which once represented far more labor-intensive processes that now can be automated. CP businesses can realize some margin benefits in these areas as they look to mitigate the macro-level uncertainties of a potentially protracted trade war. Going forward, clients need to identify and proactively mitigate the impacts of tariffs on their businesses by prioritizing potential avenues for cost efficiencies, including process automation and enterprise resource planning.
Financial sponsors grabbed their greatest share of M&A activity in the consumer space of the past 5 years at 37 percent in Q4.

After investing $74 billion in Q3, PE investors pulled back considerably to $36 billion.

The $227 billion spent in aggregate this year topped last year’s total of $197 billion but fell short of the record set in 2015.

Deal counts in retail fell by 27 percent year-over-year in 2018, with Q4 posting a multiyear low in terms of quarterly transaction volume.

Capital invested in retail companies ticked up from Q3 by about a third to nearly $12 billion.

12 percent increase in total deal value for 2018 over 2017 levels.

Eclipsing $200 billion for the quarter, transaction sizes kept deal value near record highs in Q4.

Transaction volume fell to its lowest quarterly level in 5 years, representing under 600 deals.

50 percent decline in deal volume over the past year.
PRIVATE EQUITY EXPANDS ITS REACH

PE investors have become a significant presence in consumer M&A relative to strategics, even as dealmaking has fallen considerably. Financial sponsors wrapped up a greater portion of overall volume in Q4 than in any other quarter in the past five years. At the same time, however, activity fell for a fourth straight quarter to its lowest level for the same period. The $227 billion that PE investors spent in 2018 topped last year’s total of $197 billion. Meanwhile, PE-sponsored exits fell for the third straight year, returning to levels last seen in 2011.
RETAIL EXTENDS MULTI-YEAR DECREASE IN ACTIVITY

Although deal counts in retail fell by 27 percent year-over-year in 2018, with Q4 posting a multi-year low in terms of transaction volume, capital invested into the space ticked up from Q3 to nearly $12 billion. That recovery pushed deal value over 2017 levels by 12 percent. Meanwhile, the massive combination of European eyewear makers Essilor and Luxottica masked an otherwise average Q4 for apparel & accessories M&A at some $7 billion in aggregate transaction value.
CONSUMER M&A DEAL FLOW REACHES 5-YEAR LOW

CP M&A dipped below 600 transactions in Q4, extending the decline in volume into a fourth consecutive quarter. Activity in Europe fell for the seventh straight quarter to its lowest level in five years. North America hit a new low in Q4 with fewer than 400 transactions. Although softening volume dates back several years, nearly 600 deals were closed in Q4 2017. Meanwhile, median deal size continued to climb. Add-ons represented a favorite among financial sponsors.
Focusing on the middle market, RSM US provides integrated transaction advisory, tax, assurance and consulting services. Our work with 3,600 consumer products companies gives us a deep understanding of the key trends impacting the industry. In addition, we have performed due diligence on more than 2,200 deals in the past five years, nearly 200 of which were consumer products transactions. This in-depth knowledge provides our private equity and strategic buyer clients with industry-specific due diligence considerations.